No. 85556-1

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

TESORO REFINING AND MARKETING COMPANY,

Respondent,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Petitioner.

BRIEF OF AMICUS CURIAE ASSOCIATION OF WASHINGTON BUSINESS

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes and Legislative Materials

Other Authorities

I. INTRODUCTION

It's no secret, at least among legislative bill drafters, that so long as the Legislature purports to "clarify" the "original intent" of an enactment against a contrary interpretation by a court or agency, constitutional principles may allow such a "clarification" to be applied not only prospectively, but also retroactively. Among other issues, this case presents a compelling question on retroactivity in matters of taxation: how far back may the Legislature reach, tossing aside the reliance of taxpayers on settled interpretations, without straining credulity and ultimately violating due process? How far is too far?

Whether under federal principles fleshed out in *Carlton* or the independent analysis of this court stretching back as far as *Pacific Tel. & Tel.*, the nearly quarter-century of retroactivity proposed by Senate Bill 6096 (2009) – or even the seven to nine years of retroactivity as applied to Tesoro -- simply goes too far.

For amicus curiae Association of Washington Business ("AWB"), this issue is not about "bunker fuel" or oil refineries. AWB's predominately small business membership can live or die by day-to-day application of long-standing interpretations of state tax law. For these taxpayers, for whom the maxim "the power to tax is the power to destroy" is no mere nicety plucked from constitutional history books -- it is a matter of substantial concern when the Legislature and Department of Revenue, especially in times of economic calamity and persistent state revenue shortfall, join together to launch expeditions into the nooks and crannies of Title 82 RCW finding the urgent need to "clarify" that the Legislature really meant to impose greater levels of taxation years or even decades ago regardless of taxpayer reliance on contrary interpretations. This case presents the court an excellent opportunity to revisit and update its longstanding line of cases on the permissible scope of such "clarifications."

II. IDENTITY AND INTEREST OF AMICUS CURIAE

Founded in 1904, AWB is the state's oldest and largest general business membership federation, acting as the state's chamber of commerce and representing the public policy interests of the statewide business community before the legislative, executive, and judicial branches of the state. AWB's 7,500 members employ over 650,000 individuals in Washington, nearly one-third of the state's workforce. This membership ranges from highly visible and iconic Washington-based corporations who do business around the state and around the globe, as well as very small storefronts, manufacturers, builders, developers, and service providers from every corner of the state. Eighty-five percent of AWB members employ fewer than 10 employees.

AWB members share in common taxpayer status under the various business tax laws of this state and its political subdivisions. AWB therefore frequently appears as a party or amicus curiae in state and local tax cases of consequence to its membership, reinforcing the organization's interest in the stable, predictable, and certain interpretation and application of tax laws and rules.

III. ISSUES OF CONCERN TO AMICUS CURIAE[1]

Whether the Court of Appeals was correct in holding that it violates due process for a legislative change in tax law to be retroactive for a period as long as 24 years? *Cf. Pet. for Rev.* at 1, Issue 2; *Answer to Pet.* at 5, Issue 2.

IV. STATEMENT OF THE CASE

This case turns on statutory interpretation and a legal determination of the permissible bounds of statutory retroactivity. No material facts appear to be in dispute. For brevity's sake, AWB adopts, as if set forth herein, the Statement of the Case provided by Tesoro in its Answer to the Petition for Review at 5-8.

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[1] AWB also agrees with Tesoro's position on the statutory interpretation question surrounding former RCW 82.04.433. That issue, however, was more than adequately

V. ARGUMENT

THE COURT OF APPEALS' RETROACTIVITY HOLDING SHOULD BE AFFIRMED.

At the outset, AWB would point out one instance where it agrees with petitioner Department of Revenue and disagrees with respondent Tesoro. At the petition stage, the Department contended this case presents a matter of substantial public importance, *Pet. for Rev.* at 19, while Tesoro countered, "[n]or is it likely that the Legislature would be so brazen as to make another run at imposing a retroactivity period as patently indefensible as the 24 year period tried out here." *Ans. to Pet.* at 20. Given the likelihood of another legislative session in 2012 centered around a multi-billion dollar shortfall in general fund revenue to the state, and the pressure to maximize tax receipts however possible, business taxpayers would rather not take their chances. Indeed this case presents a question of substantial public importance – about which presumably the court agreed in granting review – and the court needs not only reach the retroactivity issue but reiterate its clear and longstanding guidance to the Department and Legislature on it.

In doing so, the Court of Appeals' clear logic should weigh heavily. Dismissing the Department's defense of the retroactivity clause

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addressed by both the Court of Appeals in its decision and Tesoro in its briefing below and in supplement to this court. AWB's amicus brief will focus on retroactivity.

of the 2009 amendment to RCW 82.04.433, the Court of Appeals held "that the 24-year period is well beyond the limit of permissible retroactivity and retroactive enforcement of the amendment would violate due process." *Tesoro Refining & Marketing Co. v. Dept. of Revenue*, 159 Wn. App. 104, 120, 246 P.3d 211 (2010).

1. *Carlton* Is Entirely Distinguishable

In reaching that holding, the court followed two parallel tracks. First, obliterating the Department's "misguided" reliance on *United States v. Carlton*, 512 U.S. 26, 114 S. Ct. 2018, 129 L. Ed. 2d 22 (1994), the court correctly analyzed *Carlton* to stand for five basic hallmarks of permissible retroactive tax legislation:

- The curative amendment is prompt, *Carlton*, 512 U.S. at 32;
- The curative amendment proposes only a modest period of retroactivity, *Id.*;
- Congress did not act with an improper motive, such as targeting a particular taxpayer, *Id.*;
- The taxpayer had actual or constructive notice that the tax statute would be retroactively amended, *Id.* at 30; and
- The taxpayer did not reasonably rely to his detriment on pre-amendment law. *Id.*

Contrasting the 14 month period of retroactivity at issue in *Carlton* with the 24-year period at issue here, the Court of Appeals correctly determined the Legislature's action was neither prompt nor modest. *Tesoro*, 159 Wn. App. at 119. Further, it did not escape the court's notice that SB 6096 was introduced in ostensible reaction to the trial court's consideration of this case and ushered with conspicuous speed through the legislative process to become effective on the eve of summary judgment. The court reasonably deduced such circumstances "evidence[] the type of improper taxpayer targeting identified by the *Carlton* Court." *Id.* Finally, the Court of Appeals pointed out that taxpayers like Tesoro had undisputedly relied upon the pre-2009 interpretation and application of RCW 82.04.433, and that the 2009 change would be "novel" – without notice – to such taxpayers. *Id.* In sum, the Court of Appeals found *Carlton* entirely distinguishable, as should this court.

2. Independent State Law Analysis Should Control

The second and more important track, however, was the Court of Appeals' independent state analysis. It is important to note that the Court of Appeals' holding was presented "under Washington law." *Tesoro*, 159 Wn. App. at 119. Starting with *State v. Pac. Tel. & Tel. Co.*, 9 Wn.2d 11, 17, 113 P.2d 542 (1941), this court was presented with the question whether the Legislature, in a 1939 enactment, "had the right to provide for the collection of the tax as far back as April 30, 1935." *Pac. Tel. & Tel.*, 9 Wn.2d at 17. Relying on *Welch v. Henry*, 223 Wis. 319, 326, 271 N.W. 68 (1937) for the principle that tax retroactivity could permissibly extend back to "prior but recent transactions," the court rejected a four year period of retroactivity.

Although not discussed in the Court of Appeals decision but touched upon by Tesoro, *Supp. Br. of Resp't* at 14, n. 12, a more recent state law case offering guidance is *Japan Line, Ltd. v. McCaffree*, 88 Wn.2d 93, 558 P.2d 211 (1977). In *Japan Line*, the complaint turned on the imposition of a leasehold tax, signed into law on March 1, 1976, that was retroactive to January 1, 1976. The court was looking at a <u>two month</u> period of retroactivity. The court noted the Legislature's otherwise "broad powers" to enact tax laws are subject to "narrow and specific limits" when retroactivity is implicated. *Japan Line*, 88 Wn.2d at 96. The court allowed the two months of retroactivity, but only on a finding that given a long-running controversy over the manner of taxing the leases involved, the imposition of the tax was neither "novel" nor "unexpected." *Id.* (citing *Bates v. McLeod*, 11 Wn.2d 648, 120 P.2d 472 (1941)). Here, of course, we have a period that exceeds the contemplated retroactivity in *Japan Line* by 144 times. While neither the manufacturing nor wholesale/retail B&O tax is new, of course, the extension of the tax to receipts that were previously deductible from it is certainly "novel," as evidenced by the three prior Departmental rulings on the ability of refiners to deduct amounts derived from the sale of bunker fuel against its manufacturing B&O tax. *Tesoro*, 159 Wn. App. at 114 (discussing 1988 and two 1993 Department interpretations); *see also Ans. to Pet. for Rev.* at 7 n. 4 (same).

3. Importance to Washington Business Taxpayers

As suggested at several points above, for AWB this is no mere parochial dispute between the state tax collector and a large corporation in an oft-targeted industry. In Washington, businesses, and by necessity this means predominately small businesses, pay 52.9 percent of all taxes collected by the state and local governments, a proportionate share that perennially ranks Washington in the top ten for most taxed business communities nationwide. *See* Council on State Taxation, Total State and Local Business Taxes, State-by-State Estimates for Fiscal Year 2010 (July, 2011) at 9, available online at http://www.cost.org/Page.aspx?id=69654 (last visited Sept. 9, 2011). Our unique Business & Occupations tax is a primary driver of that statistic. Certainty and predictability in the laws, rules, interpretations, and guidance upon its various incidents, measures, credits, deductions, and exemptions, are of vital importance to our state's employers, now more than ever. Retroactive application of tax laws obviously undermines this stability. While that is a social cost the Legislature may have the limited power to impose in certain circumstances, it must be recalled that power is limited. If, by contrast, the Department prevails in its defense of a 24-year window of retroactivity, having taken fragile flight on the gossamer wings of the Legislature's purported 2009 "clarification" of a 1985 enactment, then there are essentially no limits to the Legislature's retroactive taxing power.

The Legislature will certainly take notice. Given the multi-billion dollar revenue shortfalls that have confronted the state annually since the 2009 legislative session, credits, deductions, and exemptions to the B&O tax have come in for searing criticism and scrutiny. In the 2010 legislative session, for instance, House Bills 2971, 3176, and 3191 were all proposed to amend existing tax laws to limit or repeal certain deductions, including certain sections with retroactive application. While none of the House bills were enacted, Senate Bill 6143 was enacted, which also, among other things, made retroactive amendments to certain B&O deductions until the bill was repealed by the voters in Initiative 1107 (2010). The political pressure for similar measures in 2012 and beyond will certainly exist as the state's revenue collection continues to falter in a down economy. A clear holding from this court, drawing on its pre-existing body of precedent on the limited range of permissible retroactivity in tax statutes, is essential.

VI. CONCLUSION

Any period of tax retroactivity is disruptive to businesses seeking predictability and finality with respect to their tax obligations. While some limited period of retroactivity may be permissible under the federal and state constitutions, clearly that period is limited. In applying and re-affirming state case law on permissible tax retroactivity, this court should closely follow *Japan Line* as illustrating a permissible period of retroactivity: no more than a matter of months, and only under comparable circumstances, such as a clear anticipation of change in law by the affected taxpayers.

In this case, a 24-year period, or even a nine year period of proposed retroactivity, following a novel "clarification" of existing law, is so far outside the bounds as to be outrageous. The Court of Appeals correctly rejected the Legislature's effort at such a long, unjustified reach-back. Its well-reasoned decision should be affirmed.

Respectfully submitted this 12th day of September, 2011.

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